

Message Text

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ACTION EUR-25

INFO OCT-01 ADP-00 AID-20 EB-11 NSC-10 RSC-01 CIEP-02

TRSE-00 SS-15 STR-08 OMB-01 CEA-02 L-03 H-03 PA-03

PRS-01 USIA-15 CIAE-00 COME-00 FRB-02 INR-10 NSAE-00

XMB-07 OPIC-12 LAB-06 SIL-01 RSR-01 /160 W

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R 151313Z AUG 73

FM AMEMBASSY BONN

TO SECSTATE WASHDC 6845

C O N F I D E N T I A L SECTION 01 OF 02 BONN 11627

DEPARTMENT PASS TREASURY AND FEDERAL RESERVE

E.O. 11652: GDS

TAGS: EFIN, GW

SUBJECT: BUNDESBANK VIEWS ON RECENT CREDIT DEVELOP-
MENTS AND THE GOVERNMENT'S NEW DRAFT
BUNDESBANK LAW

1. SUMMARY: BUNDESBANK OFFICIALS REMAIN UNIMPRESSED BY SCATTERED SIGNS OF SOME ECONOMIC SLOWDOWN AND DETERMINED TO MAINTAIN TIGHT CREDIT POLICIES, WHILE AVOIDING THE RECENT ERRATIC RATE MOVEMENTS ON THE MONEY MARKETS. THE BUNDESBANK IS UNHAPPY WITH GOVERNMENT PROPOSALS TYING THE USE OF CREDIT CEILINGS AND A NEW "ACTIVE" RESERVE REQUIREMENT TO GOVERNMENT CONCURRENCE. THE BUNDESBANK WELCOMES PROPOSALS TO TIGHTEN MINIMUM RESERVE REQUIREMENTS FOR BRANCHES OF FOREIGN BANKS. END SUMMARY

2. DURING A RECENT VISIT TO FRANKFURT THE FINANCIAL ATTACHE FOUND BUNDESBANK OFFICIALS GENERALLY UNIMPRESSED BY SOME SCATTERED RECENT SIGNS OF A SLOWDOWN IN THE GERMAN BOOM AND DETERMINED TO STICK TO THEIR TIGHT MONETARY POLICIES. ON THE OTHER HAND
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NO BUNDESBANK OFFICIAL TALKED IN TERMS OF A FURTHER

TIGHTENING IN THE IMMEDIATE FUTURE DESPITE OF THE ADDITIONAL LEEWAY PROVIDED GERMAN MONETARY POLICY BY INTEREST RATE DEVELOPMENTS ABROAD. BOTH BUNDESBANK OFFICIALS AND PRIVATE BANKERS, HOWEVER, EXPECTED THE GERMAN MONEY MARKET TO SEASONALLY TIGHTEN IN SEPTEMBER WHICH IS A MAJOR TAX MONTH.

3. BUNDESBANK OFFICIALS DID NOT FORESEE THE RECENT CREDIT CRUNCH AND ARE ATTEMPTING TO IMPROVE THEIR METHODS OF PREVENTING SUCH EXTREME AND ERRATIC MOVEMENTS IN GERMAN MONEY MARKET RATES WHICH THEY ATTRIBUTE ALMOST EXCLUSIVELY TO THE GERMAN SYSTEM OF REQUIRING MONTHLY AVERAGE MINIMUM RESERVE HOLDINGS. GERMAN BANKS HAVE TO HOLD DURING A MONTH A DAILY AVERAGE OF MINIMUM RESERVES EQUAL TO THE DAILY AVERAGE OF LIABILITIES SUBJECT TO RESERVES DURING THE PERIOD FROM THE 15TH OF THE PREVIOUS TO THE 15TH OF THE CURRENT MONTH. WHEN TOWARD THE END OF THE MONTH BANKS DISCOVER THAT THEY ARE SHORT OF THIS AVERAGE, THEY HAVE TO INCREASE RESERVES VERY DRASTICALLY DURING THE LAST FEW DAYS IN ORDER TO PUSH UP THEIR MONTHLY AVERAGE. WHEN THE BANKING SYSTEM AS A WHOLE FINDS ITSELF SHORT OF REQUIRED MINIMUM RESERVES MONEY RATES SKYROCKET. LAST MONTH EVERYONE APPARENTLY MISCALCULATED. COMMERCIAL BANKS MAY ONLY HAVE BECOME FULLY AWARE OF THE FULL EXTENT OF THEIR LIABILITIES TOWARD THE VERY END OF THE MONTH BECAUSE OF DEFICIENCIES IN THE SPEED OF THE REPORTING SYSTEM FROM THEIR BRANCHES. IN ADDITION, COMMERCIAL BANKS WERE UNDER GREAT PRESSURE TO CONTINUE TO EXPAND CREDIT BECAUSE OF THEIR LEGAL COMMITMENTS UNDER CREDIT LINE AGREEMENTS (FOR WHICH CUSTOMERS PAY A CHARGE AMOUNTING TO BETWEEN 3/4-4 PERCENT PER ANNUM). THE BUNDESBANK TRIED TO EASE MONEY MARKET CONDITIONS THROUGH ITS SPECIAL LOMBARD CREDIT, BUT FOUND THAT COMMERCIAL BANKS DID NOT HAVE SUFFICIENT DISCOUNTABLE PAPER SINCE THERE SEEMS TO HAVE BEEN SOME SWITCH FROM BORROWING AGAINST SUCH PAPER TO INSTEAD UTILIZING CREDIT LINES.

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4. THE BUNDESBANK IS NOW CONSIDERING EXPANDING THE COLLATERAL ACCEPTABLE FOR ITS SPECIAL TEN DAY CREDIT TO POSSIBLY INCLUDE BONDS, ETC., AND THUS HOPES TO AVOID FUTURE CREDIT CRUNCHES OF THIS MAGNITUDE. ON THE OTHER SIDE, IT IS OFFERING TEN- AND FIVE-DAY PAPER TO COMMERCIAL BANKS TO PREVENT MONEY MARKET RATES FROM SINKING BELOW THE

DISCOUNT RATE (SEE BONN 11607). IT FEELS IT CANNOT
OFFER SUCH PAPER ABOVE THE DISCOUNT RATE TO AVOID
BANKS BORROWING MONEY ON DISCOUNT TO INVEST IN
MORE PROFITABLE BUNDESBANK PAPER. OFFICIALS ARE,
HOWEVER, ALSO CONSIDERING WHETHER IN THE LONGER

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ACTION EUR-25

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C O N F I D E N T I A L SECTION 02 OF 02 BONN 11627

RUN CHANGES IN THE MINIMUM RESERVE SYSTEM ARE
DESIRABLE.

5. BUNDESBANK OFFICIALS ARE UNHAPPY WITH THE
PROVISION IN THE GOVERNMENT'S DRAFT BUNDESBANK
REFORM LAW WHICH REQUIRES GOVERNMENT CONCURRENCE
TO THE USE OF THE TWO NEWLY TO BE CREATED INSTRU-
MENTS OF CREDIT CONTROL THROUGH CREDIT CEILINGS
AND A SPECIAL RESERVE REQUIREMENT FOR ADDITIONAL
CREDIT EXPANSION. IT IS NOT YET CLEAR IF THE
BUNDESBANK WILL FORMALLY OPPOSE THESE
PROVISIONS AND INDICATE THAT IT WOULD PREFER TO
SEE THEM ELIMINATED FROM THE BILL RATHER THAN TO
HAVE THEIR USE MADE SUBJECT TO GOVERNMENT CONCURRENCE.

6. THE BUNDESBANK, ON THE OTHER HAND, WELCOMES
A PROVISION OF THE BILL PROVIDING THAT BRANCHES

OF FOREIGN BANKS IN THE FRG SHALL FOR MINIMUM
RESERVE PURPOSES BE TREATED AS IF THEY WERE
INDEPENDENT ENTITIES. THIS WOULD RESULT IN THE
GROSS LIABILITIES OF SUCH BRANCHES TO THEIR
PARENTS BECOMING SUBJECT TO MINIMUM RESERVES RATHER
THAN AS AT PRESENT ONLY THE BALANCE BETWEEN
LIABILITIES TO AND CLAIMS ON THE PARENT.
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